

STATISTICAL STUDY FROM THE AUDIT PROCESS

This summary was compiled by the Department's Audit Division. The information is based on 100% of the audits completed, taxpayers assisted and special projects conducted by the Department during Fiscal Year 1998. The information on the following pages satisfies the requirements set forth by IC 6-8.1-14-4(2).

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Taxpayers Served In District Offices

Taxpayer assistance is available in all district offices. Each office has a district office manager who performs taxpayer service functions as well as other office responsibilities. Some offices have an assistant district office manager and/or a field investigator who supports taxpayer assistance. Field investigators also perform collection functions in their districts. Intermittent employees are available throughout the year to support taxpayer assistance.

The "Taxpayer Assistance Report" (Exhibit A) provides the number of taxpayers assisted (in person and by telephone) and the amount of money collected and assessed in each office. Exhibit A reveals during Fiscal Year 1997 district offices assisted 197,674 taxpayers in person and 307,021 taxpayers through telephone contact. Total taxpayers served by the district offices is 504,695. The district office in Kokomo served 29,219 taxpayers in person, the highest number of any district office. The Merrillville District Office served 24,848 taxpayers in person, the second highest total.

The Merrillville District Office served 64,597 taxpayers by telephone while the Bloomington District Office served 34,125 taxpayers by telephone. This was the highest number of telephone contacts among the district offices, representing 21% and 11% respectively. The Merrillville District Office served a total of 89,445 taxpayers by telephone and walk-in assistance while Kokomo served 60,569 taxpayers by telephone and walk-in assistance.

"Taxpayer Assistance/Special Project Statistics" (Exhibit B) provides the number of hours devoted by field auditors in the district offices to assist taxpayers and conduct special projects. The exhibit reveals that 16,153 auditor hours were channeled in this direction.

Audit Division's Special Projects

One special project pursued by the Audit Division during the 1998 Fiscal Year deserves mention: Project Comply IV. The Comply IV project is summarized below.

Project Comply IV

This project commenced at the conclusion of Project Comply III and was conducted statewide. These audits identified candidates that were usually small and would normally not meet the criteria for a regular audit examination. The results of Project Comply IV are:

Audits Completed	994
Assessments	\$1,255,151

Refunds	\$ 123,667
Average Hours Per Audit	19.7

Exhibits C, D, and E (pages 38-40) contain the amount of assessments (refunds) and violations of the gross income tax, sales tax and adjusted gross income tax administrative rules, respectively. "Total assessments" for any tax type represent gross assessments less amounts refunded.

Statute/Rules Violated By Taxpayers

Gross Income Tax Violations

The most frequently violated gross income tax rule found in Exhibit C is 45 IAC 1-1-96. This rule defines gross receipts from services. Such receipts include all amounts charged for labor and expenses that form an integral part of the completion of the contract. Violations of this rule accounted for 12.03% of all violations of the gross income tax rules in the statistics. This was also the most frequently violated rule in the previous three studies, accounting for 12.26%, 12.07% and 12.76% of the violations during those fiscal years.

The second most frequently violated gross income tax rule is 45 IAC 1-1-120. This rule defines taxable and nontaxable shipments of goods into Indiana from other states and accounts for 7.71% of the violations of the gross income tax rules. Rule 45 IAC 1-1-120 was also the second most frequently violated rule in our 1994 and 1996 studies but ranked third for the 1997 study.

Ranking third in Exhibit C and accounting for 6.39% of the gross income tax rule violations is Rule 45 IAC 1-1-8. This rule defines receipts to mean the entire gross income or gross receipts derived from all sources and which are actually or constructively received by a taxpayer, credited to the taxpayer or paid to a creditor by another party. This rule ranked as the second most violated rule in the 1997 study with 5.65% rate of error.

Sales/Use Tax Violations

Analysis of Exhibit D and previous statistical studies reveals the three most violated sales and use tax rules are the same for fiscal years 1998, 1997 and 1996. The rules are shown below with their percentage of total violations for the three years.

	<u>1998</u>	<u>1997</u>	<u>1996</u>
Number one 45 IAC 2.2-3-4	16.52%	18.87%	19.15%
Number two 45 IAC 2.2-3-20	12.55%	11.61%	13.77%
Number three 45 IAC 2.2-5-8	10.20%	10.71%	9.96%

Rule 45 IAC 2.2-3-4 imposes use tax on “tangible personal property, purchased in Indiana, or elsewhere in a retail transaction, and stored, used, or otherwise consumed in Indiana . . . unless the Indiana state gross retail tax (sales tax) has been collected at the point of purchase.” This rule was violated 687 times during the 1998 Fiscal Year as opposed to 775 times for the 1997 Fiscal Year.

Rule 45 IAC 2.2-3-20 states that if the seller of tangible personal property for storage, use, or consumption in Indiana fails to collect the appropriate tax, the purchaser of such property must remit use tax directly to the Department. This rule accounted for 522 violations for the 1998 Fiscal Year while 477 violations occurred for the 1997 Fiscal Year.

The third most violated sales and use tax rule is 45 IAC 2.2-5-8. This rule clarifies the sales and use tax by providing examples of taxable and nontaxable sales of manufacturing machinery, tools, and equipment used in direct production and other activities. The failure of taxpayers to comply with this rule accounts for 424 of the 1998 fiscal year violations. This rule accounted for 440 violations during the 1997 fiscal year.

Corporate Adjusted Gross Income Tax Violations

Exhibit E reveals that corporate taxpayers violated the adjusted gross income rule, 45 IAC 3.1-1-97, more than any other rule. This rule addresses the returns and reports that must be filed by adjusted gross income tax withholding agents. Violations of this rule accounted for 20.92% of the total violations. This was also the most violated rule in the 1996 and 1997 studies and accounted for 18.87% and 22.14% of the total violations.

Rule 45 IAC 3.1-1-8 was the second most frequently violated rule under this study. This rule states that “taxable income” as defined in the Internal Revenue Code is modified in several ways to arrive at Indiana adjusted gross income. These violations account for 16.58% of the total violations. This rule was also the second most frequently violated adjusted gross income tax rule in 1996 accounting for 15.9% of the total and for 1997 representing 17.35% of the total violations.

The third most frequently violated rule found in Exhibit E is 45 IAC 3.1-1-9. This rule deals with the adoption of modifications as defined in the Internal Revenue Code. More specifically, it allows a net operating loss as a deduction in computing Indiana Adjusted Gross Income (IRS Code Section 172). This rule accounts for 7.07% of the violations of adjusted gross income tax rules. The 1997 violations for this rule also ranked third with 7.96%.

Amount Of Tax Assessed For Violations

The amount assessed for each of these violations and the percentage of the amount to total assessments is presented below:

Gross Income Tax:

Violation	Amount Assessments	% Of All Assessments
45 IAC 1-1-96	\$1,486,127	9.94%
45 IAC 1-1-120	*(\$1,475,339)	*
45 IAC 1-1-8	\$497,954	3.33%

**Denotes Refund*

Sales/Use Tax:

Violation	Amount Assessed	% of All Assessments
45 IAC 2.2-3-4	\$4,119,135	18.19%
45 IAC 2.2-5-8	\$7,799,497	34.43%
45 IAC 2.2-3-20	\$2,095,066	9.25%

Corporate Adjusted Gross Income Tax:

Violation	Amount Assessed	% of All Assessments
45 IAC 3.1-1-97	\$1,247,953	7.70%
45 IAC 3.1-1-8	\$2,031,962	12.53%
45 IAC 3.1-1-9	*(\$1,739,199)	*

**Denotes Refund*

Industry Or Business Most Frequently In Violation

For the sixth consecutive time, taxpayers engaged in manufacturing most frequently violated the gross income tax rules. This group committed 177 violations or 32.27% of the total violations. The gross income tax rule most frequently violated by this group of taxpayers was 45 IAC 1-1-120. This rule defines taxable and non-taxable shipment of goods into Indiana from other states.

The second largest number of gross income tax violations was committed by taxpayers in wholesale and retail trade. This group committed 154 infractions or 28.95% of the total violations. Wholesalers and retailers were the second most frequent violators of these rules in the 1994, 1996 and 1997 studies. Rule 45 IAC 1-1-120 was most frequently violated by this group of taxpayers during Fiscal Years 1998 and 1997.

As in the previous seven years, wholesalers and retailers were the most frequent violators of the sales and use tax rules. The statistics indicate 1,531 violations or 36.82% of the total sales and use tax violations. The rule most frequently violated by these taxpayers was 45 IAC 2.2-3-4. As previously noted, this was the most violated sales and use tax rule in the study.

Continuing the correlation to the previous seven years, manufacturers were the second most frequent violators of the sales and use tax rules. There were 1,007 violations committed by this group representing 24.22% of the total violations. The rule most frequently violated by manufacturers was 45 IAC 2.2-5-8, which clarifies the sales and use tax by providing examples of taxable and nontaxable sales of manufacturing machinery, tools, and equipment used in direct production and other activities.

Wholesalers and retailers, with 441 infractions, were the most frequent violators of adjusted gross income tax rules. This figure represents 39.95% of the total adjusted gross income tax violations.

Manufacturers were the second most frequent violators of the adjusted gross income tax rules. Manufacturers committed 305 infractions or 27.63% of the adjusted gross income tax violations.

The wholesalers and retailers most violated rule 45 IAC 3.1-1-97 which addresses returns and reports filed by adjusted gross income tax withholding agents. The rule most violated by the manufacturers was 45 IAC 3.1-1-8 which deals with IRS Code modifications to arrive at Indiana adjusted gross income.

Special Tax Violations

Exhibit F provides the number of special tax rule violations and the amount of special tax assessments and refunds.

Article VII of the International Fuel Tax Agreement (IFTA) was the most frequently violated special tax item in the study. It specifies jurisdictions may require payment of motor fuels taxes on retail sales of motor fuels delivered into the fuel tank that propels the motor vehicle. Article VII was violated 145 times and yielded \$101,056 in refunds for the State of Indiana. This represents 25.53% of total violations.

The exhibit also reveals that Article III of the International Fuel Tax Agreement (IFTA) was the second most frequently violated section of the special tax statutes. This section specifies the taxable event is the consumption of motor fuels in the propulsion of qualified motor

vehicles, except fuel consumed that is exempt from taxation by a jurisdiction. All motor fuel acquired that is normally subject to consumption tax is taxable unless proof to the contrary is provided by the licensee. This section was violated 138 times accounting for 24.30% of the total violations. These violations resulted in assessments of \$176,775 and refunds of \$8,580.

The taxpayer group most frequently in violation of the special tax statutes and IFTA Articles was the transportation industry. This group committed 321 violations accounting for 56.51% of the total infractions. Article VII of the International Fuel Tax Agreement was most frequently violated by the transportation industry.

Miscellaneous Taxes and Penalties

Exhibit G provides the number of violations and assessment amounts of the following:

Financial Institutions Tax
Penalty and Interest Assessments
Food and Beverage Tax
Innkeeper's Tax

A review of this exhibit reveals that IC 6-3-2-2 was violated 26 times. This code section addresses corporations and nonresidents adjusted gross income derived from sources within Indiana. These violations yielded \$121,006 in net assessments.

The 23 violations of IC 6-2.1-3-24.5 yielded a total of (\$133,182) in refunds. This code section defines corporations that qualify to file as Special Corporations.

Number of Years in the Audit Period

The audit period was three years.

Use of Professional Tax Preparation Assistance

The services of professional preparers were used in the preparation of 75.5% of the corporate income tax returns and 11% of the sales tax returns. These findings remain consistent with the previous years' reports.

Filing Of Appropriate Tax Returns By Taxpayers

Rule 45 IAC 3.1-1-92 (Exhibit E) requires qualifying corporations to make estimated tax payments. Taxpayers in violation of this rule either failed to file estimated income tax returns or failed to remit the appropriate amount of tax. For the fiscal year ending in 1998, the study indicates 23 violations of this rule, resulting in net assessments in the amount of \$44,360 and refunds totaling \$156,716.

Indiana Code 6-8.1-10-2.1 (Exhibit G) was violated 1 time. This section specifies the penalty to be imposed if a taxpayer fails to file an appropriate return or pay the full amount of tax due. Violations of this section in the previous year's report numbered 5.

EXHIBIT A	Taxpayer Assistance Report - Fiscal Year 97 - 98												
	Audit Division District Offices												
	South Bend	Fort Wayne	Lafayette	Kokomo	Muncie	Terre Haute	Bloomington	Columbus	Clarksville	Evansville	Merrillville	Totals	
Walk In Assistance	17,486	15,280	19,406	29,219	7,253	12,622	24,287	15,941	10,012	21,320	24,848	197,674	
Telephone Assistance	24,259	24,503	20,816	31,350	20,748	18,525	34,125	15,287	20,494	32,317	64,597	307,021	
Totals	41,745	39,783	40,222	60,569	28,001	31,147	58,412	31,228	30,506	53,637	89,445	504,695	
Collected/Assessed	1,953,525	870,153	829,899	3,246,895	1,371,127	619,315	1,629,501	1,012,360	2,129,583	1,660,482	2,152,892	17,475,732	

Exhibit B	Taxpayer Assistance/Special Project Statistics	
	Field Auditors	
	Regions	Total Hours
Region I	(South Bend, Fort Wayne, Merrillville)	5,007
Region II	(Lafayette, Kokomo, Muncie)	4,294
Region III*	(Indianapolis)	1,393
Region IV	(Terre Haute, Bloomington, Columbus, Clarksville, Evansville)	3,524
Region V	(Out Of State Auditors)	0
Region VI	(Special Tax Auditors)	1,935
	Totals	16,153
	*Represents special projects only. Taxpayer assistance provided by	
	Taxpayer Services Division	
	This field auditor information was gathered using information from regional	
	reports indicating hours charged to GA-30 number for ADM-Special Projects	
	and ADM-TSD	

